

DEPARTMENT OF STATE REVENUE

**LETTER OF FINDINGS NUMBER: 97-016IFTA
IFTA**

For The Period: 1993 through 1995

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ISSUES

I. Tax Administration: Penalty

Authority: IC 6-6-4.1-20; IC 6-8.1-10-4; 45 IAC 15-11-4; 45 IAC 15-5-7(3); IC 6-8.1-10-2.1

The taxpayer protests the assessment of 100% fraud penalty.

STATEMENT OF FACTS

The taxpayer is engaged in the trucking industry, transporting products. The Indiana Department of Revenue audited the taxpayer in the early part of 1997. The auditor found several "variances" and errors in the taxpayer's records, including alterations in the information on the taxpayer's IFTA summaries (and also alterations to non-IFTA jurisdictions). The auditor noted that tax liability was reduced by these alterations. The auditor also found that the taxpayer did not use any internal controls to reduce tax errors. Based upon these variances and errors, and the fact that the taxpayer subtracted out Indiana toll road miles, a 100% fraud penalty was imposed. More facts will be provided below as needed.

I. Tax Administration: Penalty

DISCUSSION

The taxpayer protests the imposition of a 100% fraud penalty. As the taxpayer states in a letter, dated September 9, 1997:

I am requesting a hearing to settle the matter of the 100% penalty that your state [Indiana] is charging me. It is my understanding that the International Fuel Tax

Agreement [IFTA] is regulated by a common standard that all states must abide by.

And further:

I am aware ... that the tax owed was a mistake on our part. But I am [still] protesting the 100% penalty.

At the hearing the taxpayer explained, in its defense, that the variances and errors were based on: (1) the taxpayer's reliance on the taxpayer's bookkeeper; and (2) that toll road miles are not assessed in most other jurisdictions and that its belief was that Indiana toll road miles were not taxable. The taxpayer's basic argument is that it did not intentionally avoid taxation, and thus the 100% fraud penalty should not be imposed.

Several statutes are relevant to the Department's imposition of the 100% fraud penalty. Indiana Code 6-6-4.1-18 deals with motor fuel tax and fraud for the purpose of "reduction of liability" for tax. Further, Indiana Code 6-6-4.1-20 deals with the failure to keep proper books and records, and points to Indiana Code 6-8.1-10-4 for elaboration of the penalty. Finally, IC 6-8.1-10-4 sets out the statutory requirements for the assessment of the 100% penalty. The pertinent part of IC 6-8.1-10-4 is the following:

(a) If a person fails to file a return or to make a full tax payment with that return with the fraudulent intent of evading the tax, he is subject to a penalty.

'Fraudulent intent' is defined by 45 IAC 15-11-4:

An act is fraudulent if it is an actual, intentional wrongdoing, and the intent required is the specific purpose of evading tax believed to be owing.

There are five elements used to establish fraud: (1) Misrepresentation; (2) Scienter; (3) Deception; (4) Reliance; and (5) Injury. (See 45 IAC 15-5-7(3)). All five elements must be met by "clear and convincing evidence" to show fraud.

The Department has not met its burden regarding element of Scienter--thus an analysis of the other elements is not necessary. The Scienter element is defined in the administrative code as:

Scienter: This is a legal term meaning guilty knowledge or previous knowledge of a state of facts, such as evasion of tax, which it was a person's duty to guard against. A person must have actual knowledge of the responsibility of reporting the information under contention. However, the reckless making of statements without regard to their truth or falsity may serve as an imputation of scienter for purpose of proving fraud.

The Department's failure to meet its burden of proof regarding the Scienter element is evidenced by the Department's own reports. For instance, the Department noted that

the taxpayer did not have a computerized system, did not keep individual truck information from past quarters, and that there were many clerical errors. The Department has only shown that the taxpayer made several errors and used what can only be dubbed “sloppy” record keeping procedures.

Regarding the issue of toll road mileage, this is a contentious issue that was litigated in the early 1990's. In Area Interstate Trucking v. Indiana Dept. of State Revenue, 605 N.E.2d 272, 278 (Ind. Tax 1992), the Indiana Tax Court held that the motor carrier fuel tax “as applied to the consumption of fuel by motor carriers in operating on the Indiana toll road, offends neither the United States nor the Indiana Constitution.” Although the Department is correct on the merits of the substantive issue, namely that the taxpayer erroneously subtracted the toll road miles out, nonetheless the taxpayer may have believed that it was in comportment with the law.

Although the Department has not met its burden of proof regarding the 100% fraudulent penalty, it has shown negligence on the taxpayer's part. The negligence penalty imposed under IC 6-8.1-10-2.1 subjects a taxpayer to a ten percent penalty if the taxpayer incurs a deficiency that is due to negligence. However, the penalty shall be waived if the taxpayer shows the deficiency was due to reasonable cause and not due to willful neglect. The failure to have internal controls, the failure to be familiar with Indiana law (e.g., Area Interstate Trucking) on the issue of toll roads, the alteration of figures, and that fact that the taxpayer has been in the trucking industry for numerous years and operates in several jurisdictions shows negligence on the taxpayer's part.

The final argument that the taxpayer makes is that the International Fuel Tax Agreement (IFTA) sets the “standard” on penalties. The taxpayer's September 9, 1997, letter states:

[The IFTA] laws state that the penalty on unpaid fuel tax is \$50.00 or 10% of the tax owed which ever is greater. ... It is my understanding that [IFTA] is regulated by a common standard that all states must abide by.

The taxpayer fails to address the fact that the IFTA Articles of Agreement provide that “Nothing in the Agreement limits the authority of a jurisdiction to impose any other penalties provided by the laws of the base jurisdiction.” (See Commentary for IX.C.7 with IX.B.).

FINDING

The taxpayer's protest is sustained regarding the imposition of the 100% fraud penalty; however the taxpayer is denied regarding the lesser penalty imposition, namely, the negligence penalty.